

Unemployment Insurance Trust Fund Sub-committee:

The subcommittee makes the following observations and conclusions about the Unemployment Insurance Trust Fund and the related Future Fund:

The current unemployment insurance system was designed with the assumption that adjustments would need to be made periodically. Benefit levels are tied to wage inflation and increase each year, while income to the trust fund does not have automatic inflation factors and has remained stagnant. This system has not been materially modified since 1993.

House Bill 1027, introduced by the Committee on Commerce at the request of the Unemployment Insurance Advisory Council, is intended to reverse the effects of factors that have combined to bring the Unemployment Insurance Trust Fund to its lowest fund balance in more than a decade. Rising expenditures (unemployment benefits) without similarly rising revenues (employers' contributions) for a number of years have drastically depleted the trust fund.

If this situation was left unabated, the current situation of unemployment benefits and employers' contributions would continue to deplete the trust fund to the point where the statutory payroll surtax would trigger and all employers statewide would see a significant increase in their unemployment tax rates.

During the 80th Legislative session, the legislature passed a bill to fix certain inequities in the Unemployment System. The main goal last year was to open the dialogue between the legislature and the public about the need for the changes which are addressed in HB 1027.

Corrections to the Unemployment System in HB1027 include:

- An increase in the wage base upon which unemployment tax is calculated (2007 - \$8,500, 2008 - \$9,000, 2009 - \$9,500, and 2010 - \$10,000).
- There is an increase in the reserve ratios for negative account holders. (If a business has a negative account balance, the new reserve ratios as set forth in HB1027 and the related new tax percentages make it possible for businesses with negative accounts to move towards positive balances more expeditiously.
- Current South Dakota law has a minimum contribution rate of 0% and a maximum of 7.0%. The proposed law maintains the 0% rate and increases the maximum to 8.5%. The average contribution rate in 2007 would be 0.35% - still significantly less than surrounding states.
- The bill establishes a new interest charge penalty for all employer accounts which have been negative for 2 consecutive years.
- The surtax trigger level will be reduced from \$11 million down to \$2 million for a 3 year period of time, to allow the system time to recover before the surtax triggers on all South Dakota businesses.

These corrective actions are projected to return the trust fund to a healthy balance by Fiscal Year 2010 and avoid the statewide surtax on all businesses.

There is a connection between the Unemployment Insurance Trust Fund and the Future Fund (Contribution Fee) as they are calculated and remitted on the same quarterly Employer's Quarterly Contribution, Investment Fee, and Wage Report. As the wage base increases by HB 1027, the Future Fund would receive unintended increases as well. The estimates show that for every \$1,000 dollar increase in the wage base, the unintended benefit to the Future Fund was approximately \$1,000,000. Therefore, HB 1177 was introduced. This bill will slow this growth in the Future Fund, and as adopted, would reduce the maximum tax percentage for the Future Fund tax as the wage base increases over the next four years.

The Future Fund, as stated previously, is remitted on a quarterly basis with the Unemployment Insurance. Both the Future Fund (Contribution Rate) tax and the Unemployment Insurance tax are collected by the Department of Labor. On a monthly basis, the Department of Labor remits approximately 97% of the total collected to the Department of Tourism and Economic Development. The Department of Labor withholds about 3% of the amount collected because of an OMB Circular A-87, a federal cost accounting principle requirement. This percentage is how much the Department of Labor estimates it spends in personnel service costs in the collection of the Future Fund (Contribution Rate) tax. The amount withheld from the Department of Tourism and Economic Development offsets the Department of Labor's personnel costs.

The Department of Labor, the Unemployment Insurance Advisory Group, and the sponsors of the bills that were mentioned in this report believe that these bills will not be permanent corrections for the Unemployment Insurance Trust Fund or the Future Fund. Rather, the individuals who worked closely with these issues believe these funds need to be monitored and reevaluated every few years to ensure the Funds are moving in the right direction.

